

Message Text

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PASS TREASURY AND FEDERAL RESERVE

E.O. 11652: N/A
TAGS: EFIN, OECD
SUBJECT: MARCH 2-3 MEETING OF COMMITTEE ON FINANCIAL
MARKETS AND MARCH 1 RESTRICTED MEETING WITH BANKERS

REF: CMF/A(78)1

1. BEGIN SUMMARY. COMMITTEE ON FINANCIAL MARKETS
(CFM) DEVOTED MOST OF TWO-DAY SESSION TO TOUR D'HORIZON.
USDEL DECLINED TO RESPOND TO ATTEMPTS TO HAVE "TECH-
NICAL" DISCUSSION OF MODALITIES AND MARKET EFFECTS OF
ANY US BORROWING ABROAD OF FOREIGN CURRENCY. REVISED
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VERSION OF CONSULTANTS' STUDY ON FINANCIAL RELATIONS
WITH COMECON, RELEASED JUST BEFORE MEETING, WILL BE
DISCUSSED AT JULY SESSION. KICHLIN OF US ELECTED
VICE-CHAIRMAN. NEXT CFM MEETING JULY 6-7 EXPECTED
TO CONSIDER "BALANCE SHEET" ON US-INITIATED EFFORT
TO IDENTIFY IMPEDIMENTS TO INTERNATIONAL FLOWS OF
PORTFOLIO CAPITAL. END SUMMARY.

2. CFM MET MARCH 2-3, AFTER RESTRICTED SESSION WITH PRIVATE BANKERS MARCH 1. DE RIVAZ (SWISS NATIONAL BANK) WAS ELECTED CHAIRMAN, WITH KICHLIN (U.S. FEDERAL RESERVE) AND KJAER (DANISH NATIONAL BANK AS VICE-CHAIRMEN.

TOUR D'HORIZON

3. DOMESTIC FINANCIAL MARKETS.

A. UNITED STATES. KICHLIN AGREED THAT RISE IN US INTEREST RATES, MAINLY AT SHORT END, IS EXPECTED BY MOST MARKET PARTICIPANTS. TOTAL CORPORATE BORROWING IS UNLIKELY TO GROW FASTER THAN IN 1977. TREASURY BORROWING WILL BE HIGHER (KICHLIN NOTED THAT IN 1977, 85 PERCENT OF DEBT WAS ACQUIRED BY NON-RESIDENTS OR BY STATE/LOCAL GOVERNMENTS). FOLLOWING ENORMOUS GROWTH IN 1977, MORTGAGE LENDING WILL EXPERIENCE SOME TIGHTENING IN 1977 (DEPOSIT FLOWS TO THRIFT INSTITUTIONS ARE SLOWING), BUT THIS SHOULD NOT BE A SERIOUS IMPEDIMENT TO HOUSING SECTOR. IN RESPONSE TO QUESTIONS, US (NEWMAN) SAID EXTENT OF FOREIGN PURCHASES OF TREASURY PAPER IN 1978 COULD NOT BE PREDICTED AND INDICATED THAT THE "PROPOSED RULING" ON BANK LENDING ABROAD ISSUED BY COMPTROLLER OF THE LIMITED OFFICIAL USE

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CURRENCY ESSENTIALLY WOULD MERELY FORMALIZE PAST PRACTICES (I.E., NO SIGNIFICANT CHANGES WITH RESPECT TO APPLICATIONS OF "10 PERCENT" LENDING LIMIT).

B. JAPAN. GOJ DELS WERE UNABLE TO PROJECT DOMESTIC BORROWING IN 1978, BUT ANTICIPATED NO CHANGE IN MONETARY CONDITIONS. THEY INSISTED THAT "NO REAL BARRIER" EXISTS TO PRIVATE FOREIGN BOND ISSUES IN JAPAN AND PREDICTED A GRADUAL INCREASE. DETAILED DISCUSSION OF JAPANESE BOND MARKET -- ON BASIS OF CFM(78)3 -- POSTPONED TO JULY SESSION.

C. FRG. FINANCE MINISTRY REP (MERGENTHALER) GAVE EXTENSIVE DESCRIPTION OF GOVERNMENT'S DEBT MANAGEMENT POLICY AND SUBSEQUENTLY AGREED TO FURNISH A NOTE ON SUBJECT (SEE PARA 7 BELOW). MONETARY POLICY

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CHARACTERIZED AS HAVING TEMPORARILY LOST EFFECTIVE-
NESS, WHICH CAN BE TOLERATED IN SHORT RUN -- I.E.,
WITH IMPLICATION THAT, ONE WAY OR ANOTHER, CONTROL
WILL HAVE TO BE RESTABLISHED IF UPWARD PRESSURE ON
DM CONTINUES.

D. SWITZERLAND. REPS SAID THAT TARGET FOR MONETARY
GROWTH (5 PERCENT IN 1978) "MUST REMAIN FLEXIBLE".
RECENTLY ADOPTED RESTRICTIONS ON CAPITAL FLOWS, TO
WHICH NATIONAL BANK CAN GRANT EXEMPTIONS, WILL NOT
HAVE MAJOR IMPACT ON CAPITAL MARKETS, WHICH WILL
REMAIN VERY LIQUID IN 1978 -- INTEREST RATES SHOULD
CONTINUE TO EASE.

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E. UNITED KINGDOM. TREASURY REP (WIGGINS) CLARIFIED
POINT THAT WITH RESPECT TO STERLING EURO-BONDS EXCHANGE

CONTROLS APPLY ONLY TO BORROWINGS BY NON-RESIDENTS FOR USE ABROAD. NO QUEUEING SYSTEM EXISTS WITH RESPECT TO NEW OFFERS, ALTHOUGH INFORMATION ON PROSPECTIVE ISSUES IS DISTRIBUTED TO MINIMIZE BUNCHING. THE TREASURY IS RATHER CERTAIN THAT SOURCE OF EURO-STERLING FUNDS IS BASICALLY FROM OUTSIDE UK.

4. INTERNATIONAL CAPITAL MARKETS.

A. MARCH 1 RESTRICTED MEETING WITH BANKERS. CHAIRMAN PROVIDED ORAL SUMMARY OF MARCH 1 MEETING WHICH WILL EVENTUALLY BE REPRODUCED AS ANNEX TO MINUTES OF THIS CFM SESSION. HIGHLIGHTS WERE THAT BANKERS: (I) AGREED WITH SECRETARIAT'S VIEW (IN LATEST FINANCIAL MARKET TRENDS) ON PROSPECT FOR SOME INCREASE IN INTEREST RATES IN US BUT FELT THAT LONG-TERM RATES IN FRG MIGHT FALL FURTHER; (II) FELT THAT VOLUME OF INTERNATIONAL ISSUES WOULD BE WEAKER THAN FORESEEN BY SECRETARIAT (MAINLY IN DOLLAR SECTOR), BUT THAT SYNDICATED CREDITS COULD BE STRONGER, GIVEN REFINANCING NEEDS; (III) BELIEVED THAT GOVERNMENTS' LIMITATIONS (FORMAL OR INFORMAL) ON LENDING ARE UNLIKELY TO POSE PROBLEMS TO BANKS; AND (IV) THOUGHT THAT COMPETITION AMONG LENDERS WILL CONTINUE TO BE LIVELY AND TO AFFECT SPREADS.

B. 1978 INTENTIONS OF LARGEST OECD BORROWING COUNTRIES.

-- CANADA: IN 1978, GOVERNMENT ITSELF WILL BORROW ABROAD FOR FIRST TIME IN A DECADE. NO ARRANGEMENTS YET ON FINANCING OF \$10 BILLION PIPELINE PROJECT LIMITED OFFICIAL USE

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(LITTLE REQUIRED THIS YEAR), BUT GOC WOULD EXPECT TO DRAW ON FOREIGN MARKETS, WITH DEGREE OF RECOURSE TO EUROPEAN MARKETS DEPENDENT ON PROCUREMENT PATTERNS.

-- DENMARK: 1978 GROSS BORROWING NEEDS IN 1978 EXCEED 10 BILLION KRONOR, OF WHICH HALF ALREADY COVERED BY GOVERNMENT BORROWING (EITHER TAKEN UP OR CONTRACTED) AND THE REMAINDER BY PRIVATE INFLOWS AND OTHER PUBLIC SECTOR BORROWINGS. SOME SMALL BORROWERS HAVE DENOMINATED THEIR LOANS IN "COCKTAILS" OF CURRENCIES.

-- SWEDEN: 1978 BORROWING WILL BE OF ROUGHLY SAME MAGNITUDE AND DISTRIBUTION AS IN 1977 (21 BILLION KRONER, OF WHICH 9 BY GOVERNMENT, 1 BY CENTRAL BANK, 1 BY LOCAL AUTHORITIES, AND 10 BY PRIVATE BORROWERS).

-- AUSTRALIA, NEW ZEALAND, UK: NOTHING OF SIGNIFI-

CANCE REPORTED.

C. YEN AS INTERNATIONAL CURRENCY. JAPANESE REPS
INDICATED THAT FINANCE MINISTRY WAS SPLIT AS TO WHETHER
YEN SHOULD HAVE AN INTERNATIONAL ROLE.

5. TECHNICAL CONSIDERATIONS RELATING TO ANY USG
FOREIGN CURRENCY BORROWING ABROAD.

ALTHOUGH ISSUE NOT ON AGENDA, FRG (KLEIN OF BUNDESBANK)
RAISED QUESTION OF MEDIUM-TERM FOREIGN CURRENCY LOANS
WHICH USG SHOULD, "IN OPINION OF VARIOUS FOREIGN
OFFICIALS AND PRIVATE INDIVIDUALS", RAISE IN FOREIGN

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CAPITAL MARKETS IN ORDER "MORE APPROPRIATELY" TO
FINANCE ITS CURRENT ACCOUNT DEFICIT. KLEIN CARE-
FULLY NOTED THAT QUESTION WAS HYPOTHETICAL AND THAT
CFM COULD NOT DISCUSS WHETHER SUCH BORROWING WAS
DESIRABLE BUT ONLY TECHNICAL ISSUES SURROUNDING IT --

SUCH AS FEASIBILITY AND CONSEQUENCES FOR INTERNATIONAL MARKETS (HE NEVERTHELESS ALLUDED TO RESTORATION OF CONFIDENCE IN EXCHANGE MARKETS WHICH WOULD ALLEGEDLY BE ENGENDERED AND IMPLIED THAT PRESSURE FOR "PROTECTIONIST" POLICIES MIGHT OTHERWISE ARISE).

KLEIN THEN PROCEEDED TO OFFER REBUTTAL TO CONSTRAINTS BEING CITED (I.E., BY USG OFFICIALS). HE SAID THAT A RISE IN US INTEREST RATES WOULD AVOID (A) NEED TO PRICE SUCH ISSUES MORE ATTRACTIVELY THAN REGULAR LIMITED OFFICIAL USE

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TREASURY DEBT ISSUES AND (B) THREAT THAT HOLDERS OF EXISTING DOLLAR INSTRUMENTS, BOTH US AND FOREIGN, WOULD SELL THEM IN ORDER TO OBTAIN FOREIGN CURRENCY DENOMINATED INSTRUMENT. KLEIN EMPHASIZED THAT THIS TECHNIQUE IN CONTRAST TO EXPANDED SWAP CREDITS WOULD PREVENT EXCESSIVE EXPANSION OF DOMESTIC MONEY SUPPLY IN STRONG CURRENCY COUNTRIES. US DEL (NEWMAN) NOTED THAT THIS QUESTION WAS NOT ON AGENDA AND SAID HE WAS NOT PREPARED TO DISCUSS IT. HE ALSO POINTED OUT THAT US SPOKESMEN AT OTHER OECD MEETINGS HAD INDICATED THAT SUCH A SCHEME WOULD NOT ACCOMPLISH WHAT SOME CLAIMED IT WOULD. FRG AND NETHERLANDS REPS TRIED AGAIN TO ELICIT US REACTION BUT DID NOT PRESS ATTEMPT IN FACE OF US DEL'S REITERATION OF POSITION.

OTHER AGENDA ITEMS

6. IMPEDIMENTS TO MOVEMENTS OF PORTFOLIO CAPITAL. NOTES BY COUNTRIES IN CMF(78)8 SERIES SETTING FORTH REGULATIONS CONCERNING INVESTMENTS IN FOREIGN SECURITIES BY INSTITUTIONAL INVESTORS (12 RESPONSES RECEIVED TO DATE) WERE NOT DISCUSSED IN VIEW OF LATE ARRIVAL OF SEVERAL SUBMISSIONS. REMAINING COUNTRIES WERE AGAIN INVITED TO SUBMIT RESPONSES, AND SECRETARIAT WAS ASKED TO PREPARE "BALANCE SHEET" ON THIS EXERCISE, WHICH GREW OUT OF A US PROPOSAL AT THE 1976 MINISTERIAL, FOR DISCUSSION AT JULY CFM MEETING (AND PRESUMABLY DECISION ON WINDING IT UP OR SPECIFYING FURTHER WORK). US DEL AGREED TO THIS PROCEDURE, NOTING WE WOULD HAVE TO SUPPLEMENT OUR EARLIER SUBMISSION IN ORDER TO SPECIFY MOTIVES FOR US REGULATIONS. WITH RESPECT TO CFM UPDATING OF ITS 1974 REPORT ON IMPLEMENTATION OF COUNCIL'S RECOMMENDATION OF 14 MARCH 1972 ON LIMITED OFFICIAL USE

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INTERNATIONAL SECURITY ISSUES (CONCERNING OBSTACLES TO SALE OF EURO-BONDS IN MEMBER COUNTRIES AND USE OF MEMBER COUNTRIES' CURRENCIES FOR DENOMINATION OF EURO-BONDS), SECRETARIAT WILL CONSULT BILATERALLY WITH COUNTRIES CONCERNED AND WITH ASSOCIATION OF INTERNATIONAL BOND DEALERS. DOCUMENT ON THIS QUESTION, CMF(78)9, WAS NOT ISSUED PRIOR TO MEETING.

7. GOVERNMENT BUDGET DEFICIT FINANCING AND DEBT MANAGEMENT. DELEGATES WELCOMED SECRETARIAT'S NOTE, CMF(78)10, SETTING FORTH GENERAL QUESTIONS AND THE US AND DANISH NOTES ON THEIR PARTICULAR PRACTICES AND CONCERNS, WHICH GREW OUT OF VETTING AT PREVIOUS MEETING OF RECOMMENDATIONS CONTAINED IN "MCCRACKEN REPORT" THAT WERE RELEVANT TO CFM'S WORK. SECRETARIAT URGED OTHER COUNTRIES TO SUBMIT COMPARABLE NOTES MODELLED ON US NOTE, AND SUGGESTED THAT JULY MEETING MIGHT CONCENTRATE ON THE ISSUE, FOLLOWING WHICH IT WOULD ATTEMPT TO PULL TOGETHER ANY COMMON VIEWS. DELS URGED SECRETARIAT TO TRY TO FURNISH ITS ANALYTICAL NOTE FOR JULY MEETING.

8. COMECON COUNTRIES' RELATIONSHIPS WITH WESTERN FINANCIAL MARKETS. REVISED VERSION OF CONSULTANTS' STUDY, CMF(78)7, WAS ISSUED ONLY DAY BEFORE MEETING AND HENCE WAS NOT DISCUSSED -- CHANGES FROM DRAFT CONSIDERED AT NOVEMBER SESSION WERE SAID TO BE MAINLY IN DRAFTING. DELS WERE ASKED TO COME TO JULY SESSION PREPARED TO UNDERTAKE SUBSTANTIVE DISCUSSION AND TO

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DECIDE WHETHER TO RECOMMEND PUBLICATION OR DERESTRICT-
TION WITHOUT WIDE DISTRIBUTION (IN ANY EVENT COPIES
WOULD BE SUPPLIED TO OTHER OECD COMMITTEES).

9. STATISTICAL DATA ON CORPORATE FINANCING. CFM
TOOK NOTE OF CATALOGUE OF SOURCES OF DATA AVAILABLE
IN GERMANY, AS CITED IN CMF(78)12, AND DISCUSSED
UTILITY OF REOPENING EARLIER EXERCISE ON CORPORATE
FINANCING. DELS FROM ITALY AND NETHERLANDS EX-
PRESSED INTEREST IN RENEWED WORK; US CALLED FOR
CATALOGUE OF DATA AVAILABLE IN MAJOR COUNTRIES ALONG
LINES OF FRG COMPILATION BEFORE DECIDING WHETHER AND
HOW TO PROCEED.

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10. GROUP OF FINANCIAL STATISTICIANS (GFS). SECRE-
TARIAT (DIVOY) REPORTED ON FEBRUARY 21-24 MEETING OF
GFS, WHICH CONCENTRATED ON IMPROVEMENTS WHICH COULD
BE MADE TO "FINANCIAL STATISTICS" PUBLICATION ("GOLD
BOOKS"). SENIOR SECRETARIAT OFFICIALS REMINED CFM
THAT IT HAD RESPONSIBILITY TO GUIDE WORK OF GFS, AND
COMMITTEE ACCEPTED CHAIRMAN'S PROPOSAL TO DISCUSS
ROLE AND PRIORITY WORK AREAS OF GFS AT JULY SESSION
OF CFM.

11. REGULATIONS AFFECTING INTERNATIONAL BANKING
OPERATIONS OF BANKS AND NON-BANKS IN OECD MEMBER
COUNTRIES. SECRETARIAT REPORTED ON JANUARY 26-27 MEET-
ING OF EXPERTS. SOME MODIFICATIONS TO FIVE DRAFT
COUNTRY NOTES WERE AGREED, AND PUBLICATION BY EARLY
JUNE IS ENVISIONED. FURTHER MINOR REVISIONS
WILL BE PUBLISHED IN "FINANCIAL MARKET TRENDS". POS-
SIBLE MAJOR REVISIONS IN FUTURE (E.G., EXPANDING NOTES
TO INCLUDE REGULATORY QUESTIONS SUCH AS RESTRIC-
TIONS ON USE OF NATIONAL CURRENCY IN DENOMINATING
TRANSACTIONS OUTSIDE COUNTRY) WILL BE CONSIDERED AT
LATER DATE.

12. DEVELOPING COUNTRIES' ACCESS TO FINANCIAL MARKETS.
BROEKER OF SECRETARIAT REPORTED ON DECEMBER MEETING
OF IMF/IBRD DEVELOPMENT COMMITTEE'S WORKING GROUP WHICH
HE ATTENDED. HE SAID GROUP HAD EXPRESSED INTEREST IN
RAPID PROGRESS OF CFM'S WORK ON INTERNATIONAL BANKING
OPERATIONS AND ON IMPEDIMENTS TO PORTFOLIO CAPITAL
MOVEMENTS. NETHERLANDS DEL UNDERLINED DUTCH PREFERENCE
TO TREAT "POLITICAL" QUESTIONS CONCERNING LDC ACCESS
TO FINANCIAL MARKETS IN DEVELOPMENT COMMITTEE -- TO
EXTENT THERE WAS ANY OVERLAP WITH IT OF CFM'S WORK.
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13. IMPROVEMENT OF STATISTICS ON EURO-BONDS AND
CLASSICAL FOREIGN BONDS. SECRETARIAT RECALLED PRE-
VIOUS DISCUSSION IN CFM ON THIS SUBJECT AND REPORTED
ON FEBRUARY 28 MEETING WITH REPRESENTATIVES OF BOND
DEALERS AND SELECTED NATIONAL EXPERTS. MAIN INTEREST
OF MARKET MAKERS WAS IN DATA ON VOLUME OF OUTSTANDING
BONDS AND BREAKDOWN BY CURRENCY AND NATURE OF COUPON.

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DATA ON FOREIGN DM AND GUILDER BONDS ARE AVAILABLE, AND ASSOCIATION OF INTERNATIONAL BOND DEALERS (AIDB) CONSIDERED THAT DATA ON EURO-BONDS SHOULD BE OBTAINABLE. MAIN GAP IS IN "YANKEE" BOND AREA; AIDB COULD SUPPLY DATA ON PUBLIC ISSUES BUT NOT ON PRIVATE PLACEMENTS.

14. CONSULTANT STUDY ON INTEREST MARGINS AND COST OF INTERMEDIATION OF BANKS. SECRETARIAT REPORTED THAT STUDY IS FINALLY NEARING COMPLETION, AND COUNTRY NOTES MAY BE ISSUED IN MAY. FOLLOWING DISCUSSION WITH INTERESTED EXPERTS, POSSIBLY IN JUNE, US CONSULTANT (PROF. REVEL) WILL PREPARE FIRST DRAFT OF FULL STUDY -- HOPEFULLY FOR NOVEMBER CFM SESSION.

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15. 1979 WORK PROGRAM AND MEETING DATES. DELS REQUESTED TO SEND WRITTEN PROPOSALS FOR 1979 WORK PROGRAM (SUBJECTS AND METHODS OF WORK) OR, AT MINIMUM, COME PREPARED TO DISCUSS THIS QUESTION AT NEXT SESSION SCHEDULED FOR JULY 6-7. FALL SESSION SCHEDULED FOR NOVEMBER 9-10. BOTH WILL BE PRECEDED BY RESTRICTED MEETING WITH PRIVATE BANKERS.

16. THIS MESSAGE PREPARED AFTER DEPARTURE OF US DELS. SALZMAN

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